

ASSIGNMENT No. 01

Principle of Accounting(5401)BS A& finance Spring, 2025

Q. 1 (i): Define the term "Accounting" and its objectives.

Definition of Accounting

Accounting can be defined as a systematic process of identifying, recording, summarizing, and communicating financial transactions of a business or organization. It provides crucial information on the financial health and performance of an entity, enabling stakeholders to make informed decisions. The accounting process involves the analysis of financial data and often results in the creation of financial statements, which provide insights into revenues, expenses, assets, liabilities, and equity.

Objectives of Accounting

1. Financial Reporting

One of the primary objectives of accounting is to provide accurate and timely financial reports to external and internal stakeholders. These reports, including balance sheets, income statements, and cash flow statements, play a vital role in providing financial information to investors, management, creditors, and regulators.

2. Decision Making

Accounting assists management in making informed decisions regarding resource allocation, financial planning, and strategy development. By analyzing financial data, businesses can identify trends, forecast future performance, and assess possible outcomes before executing decisions.

3. Compliance and Regulation

Another objective of accounting is ensuring compliance with laws and regulations. Businesses must adhere to accounting standards and legal requirements, such as the Generally Accepted Accounting Principles (GAAP) or International Financial Reporting Standards (IFRS). Compliance helps avoid legal issues and promotes ethical business practices.

4. Accountability

Accounting establishes accountability within an organization. By maintaining detailed records of financial transactions, management can hold individuals and departments accountable for budget adherence and resource utilization. This accountability enhances organizational performance and fosters a culture of responsibility.

5. Performance Measurement

Accounting provides tools for measuring a company's performance over time. By examining financial metrics and ratios, such as profit margins and return on investment, stakeholders can assess the efficacy of investments and operational efficiency.

6. Resource Management

Efficient management of resources is an essential objective of accounting. By keeping track of assets, liabilities, and equity, businesses can ensure that they are utilizing resources optimally and effectively manage cash flows to support ongoing operations.

7. Risk Assessment

Accounting also aids in risk management by enabling businesses to identify financial risks and potential exposures. Through thorough analysis, managers can understand vulnerabilities in financial operations and make proactive adjustments to mitigate adverse impacts on the organization.

8. Facilitation of Audits

Accounting facilitates the auditing process by providing structured records and documented evidence of historical transactions. Audits are vital for verifying financial information and ensuring the accuracy of financial statements. Proper accounting practices streamline the audit process and enhance transparency.

9. Enhancing Business Relationships

Effective accounting helps build trust and strengthen relationships with stakeholders, including investors, creditors, and customers. By providing accurate financial information, businesses foster confidence and enhance their credibility within the market.

10. Long-Term Financial Planning

Finally, accounting supports long-term financial planning and sustainability. By analyzing historical data and current financial conditions, businesses can develop budgets, set financial goals, and create strategies for future growth and expansion.

Conclusion

In conclusion, accounting is a critical function that serves various objectives essential for effective business operations, decision-making, and regulatory compliance. It provides valuable insights into financial performance, enhances accountability, and lays the foundation for strategic planning and risk management.

Q. 1 (ii): Demonstrate how certain business transactions affect the elements of the accounting equation: Assets = Liabilities + Owner's Equity.

Understanding the Accounting Equation

The accounting equation is the foundation of double-entry accounting, reflecting the relationship between a company's assets, liabilities, and owner's equity. The equation can be expressed as:

$$\text{Assets} = \text{Liabilities} + \text{Owner's Equity}$$

This equation highlights that all assets owned by a business are financed either through borrowing (liabilities) or through the owner's investment (owner's equity).

Impact of Transactions on the Accounting Equation

1. Investment by Owner

When an owner invests cash into the business, both assets and owner's equity increase. For example, if Mr. Bilal invests Rs. 2,000,000 in cash:

$$\begin{aligned} \text{Assets (Cash)} &= \text{Liabilities} + \text{Owner's Equity} \\ \text{Rs. 2,000,000 (Increase)} &= \text{Rs. 0} + \text{Rs. 2,000,000 (Increase)} \end{aligned}$$

2. Purchase of Equipment

If the business purchases equipment for Rs. 300,000, the assets increase while cash, another asset, decreases by the same amount. This transaction does not affect liabilities.

$$\begin{aligned} \text{Assets (Equipment + Cash)} &= \text{Liabilities} + \text{Owner's Equity} \\ \text{Rs. 300,000 (Increase in Equipment)} + \text{Rs. 300,000 (Decrease in Cash)} &= \text{Rs. 0} + \text{Rs. 0} \end{aligned}$$

3. Purchase of Supplies on Credit

If supplies are purchased for Rs. 70,000 on credit, assets and liabilities both increase, as the business gains supplies without immediately paying cash.

Assets (Supplies) = Liabilities

Rs. 70,000 (Increase in Supplies) = Rs. 70,000 (Increase in Accounts Payable)

4. Truck Purchase

If a truck is purchased for Rs. 2,200,000, with Rs. 1,000,000 paid in cash and the balance financed through a note payable:

Assets (Truck) = Liabilities + Owner's Equity

Rs. 2,200,000 (Increase) = Rs. 1,200,000 (Increase in Liabilities) + Rs. 1,000,000 (Decrease in Cash)

5. Receipt of Cash for Services Rendered

When the business receives cash for completed jobs, assets increase and owner's equity also increases, reflecting additional income.

Assets (Cash) = Liabilities + Owner's Equity

Rs. 120,000 (Increase in Cash) = Rs. 0 + Rs. 120,000 (Increase in Owner's Equity)

6. Payment of Rent

When the business pays rent, cash decreases, affecting assets, and simultaneously reducing owner's equity as it reflects an expense.

Assets (Cash) = Liabilities + Owner's Equity

Rs. 75,000 (Decrease in Cash) = Rs. 0 + Rs. 75,000 (Decrease in Owner's Equity)

7. Payment to Creditors

If the business pays Rs. 240,000 to creditors, cash decreases while liabilities also decrease.

Assets (Cash) = Liabilities + Owner's Equity

Rs. 240,000 (Decrease in Cash) = Rs. 240,000 (Decrease in Accounts Payable) + Rs. 0

8. Withdrawal of Cash by Owner

When the owner withdraws cash for personal use, this transaction decreases both cash (assets) and owner's equity.

Assets (Cash) = Liabilities + Owner's Equity

Rs. 300,000 (Decrease in Cash) = Rs. 0 + Rs. 300,000 (Decrease in Owner's Equity)

Conclusion

In summary, business transactions significantly affect the elements of the accounting equation. Understanding these impacts is crucial for maintaining accurate accounting records, as they reflect the true financial position of the business and ensure that the accounting equation remains balanced.

Q. 2: What is a single-entry system of bookkeeping? Also, describe the characteristics and limitations of a single-entry system.

Definition of the Single-Entry System

The single-entry system of bookkeeping is a simplified method of recording financial transactions in which each transaction is recorded only once, either as an income or an expense, rather than in dual accounts, as is done in double-entry accounting. This system is commonly used by small businesses or sole proprietorships due to its straightforwardness and ease of use.

Characteristics of the Single-Entry System

1. Simplicity

The single-entry system is characterized by its simplicity, making it easy for small business owners to maintain. Users can record transactions without extensive accounting knowledge or training, allowing them to track income and expenses efficiently.

2. Focus on Cash Transactions

This system primarily emphasizes cash transactions and cash flow management. It records incoming cash (revenue) and outgoing cash (expenses) clearly, allowing businesses to monitor their cash position effectively.

3. Limited Financial Information

While the single-entry system provides a basic overview of financial performance through income statements, it typically does not generate comprehensive financial reports, such as balance sheets. This limitation restricts the depth of financial analysis for decision-making purposes.

4. Lack of Standardization

The single-entry system lacks standardized formats or records, leading to variability in how individual businesses maintain their accounts. This inconsistency can create challenges when comparing financial data or conducting audits.

5. Manual Record Keeping

In a single-entry system, transactions are often recorded manually in journals or ledgers. While this allows for easy tracking of individual transactions, it can lead to errors, omissions, and inefficiencies in keeping records over time.

6. Flexibility

The single-entry system allows businesses to adapt their bookkeeping methods as needed. Owners can choose to add additional details or notes for clarity without adhering to strict accounting principles.

7. Use of Cash Book

The cash book serves as the primary record for cash transactions in a single-entry system. It documents all cash inflows and outflows, summarizing the business's cash position effectively.

Limitations of the Single-Entry System

1. Incomplete Financial Picture

The most significant limitation of the single-entry system is that it does not provide a complete financial picture. Without a dual-entry system, businesses lack detailed insights into their assets and liabilities, which are important for assessing overall financial health.

2. No Internal Control Mechanism

The single-entry system has limited internal controls to prevent errors or fraud. With no checks and balances, discrepancies may go unnoticed, leading to inaccuracies in financial reporting.

3. Difficulty in Tracking Assets and Liabilities

Since the single-entry system primarily focuses on cash transactions, tracking non-cash assets and liabilities becomes challenging. Businesses may find it difficult to assess their financial position accurately, leading to poor decision-making.

4. Less Credibility to Financial Statements

Financial statements generated from a single-entry system may lack credibility and reliability when presented to external stakeholders, such as investors, creditors, or tax authorities. The absence of proper bookkeeping can undermine confidence in financial reporting.

5. Labor-Intensive

Although the single-entry system is simpler than double-entry accounting, it can still be labor-intensive for businesses with a high volume of transactions. Manual data entry increases the risk of errors and consumes valuable time that could be allocated to other business operations.

6. Limited Reporting Capabilities

Businesses utilizing a single-entry system have limited reporting capabilities, lacking comprehensive financial statements like balance sheets or cash flow statements. This deficiency restricts the ability to analyze financial performance over time.

7. Increased Risk of Omissions

The risk of omitting significant transactions is higher with the single-entry system because it relies on individual users to record all entries carefully. Missed entries can result in inaccurate financial representations, affecting decision-making processes.

8. Unsuitable for Larger Businesses

As businesses grow and complexity increases, the limitations of the single-entry system become more apparent. Larger enterprises typically require detailed and accurate financial records, making the single-entry system impractical for their needs.

Conclusion

In summary, the single-entry system of bookkeeping is a straightforward and essential method of financial record-keeping characterized by its simplicity, focus on cash transactions, and flexibility. However, it also has significant limitations, including an incomplete financial picture and inadequate controls, making it more suitable for smaller businesses or sole proprietorships. As businesses grow in complexity, the need for a double-entry accounting system becomes increasingly pertinent to ensure accuracy and credibility in financial reporting.

Q. 3: Journal Entries and Trial Balance Preparation

Background Information

Mr. Bilal has started a sole proprietorship business and needs to maintain proper records of his transactions. Below, we'll create the journal entries based on the transaction details provided for October 2024, post these to the ledger, and prepare a trial balance.

Journal Entries for October 2024

1. October 1: Investment of Cash and Equipment

Date	Particulars	Debit (Rs.)
Oct 1	Cash	2,000,000
	Equipment	300,000
	Mr. Bilal's Capital	2,300,000

2. October 3: Purchase of Supplies for Cash

Date	Particulars	Debit (Rs.)
Oct 3	Supplies	70,000
	Cash	70,000

3. October 8: Purchase of Truck

Date	Particulars	Debit (Rs.)
Oct 8	Truck	2,200,000
Cash		1,000,000
Note Payable		1,200,000

4. October 15: Purchase of Office Equipment on Account

Date	Particulars	Debit (Rs.)
Oct 15	Office Equipment	150,000
Accounts Payable		150,000

5. October 18: Payment of Rent

Date	Particulars	Debit (Rs.)
Oct 18	Rent Expense	75,000
Cash		75,000

6. October 19: Cash Received for Job Completed

Date	Particulars	Debit (Rs.)
Oct 19	Cash	120,000
Revenue from Services		120,000

7. October 22: Purchase of Supplies on Account

Date	Particulars	Debit (Rs.)
Oct 22	Supplies	260,000
Accounts Payable		260,000

8. October 23: Wages Paid to Employees

Date	Particulars	Debit (Rs.)
Oct 23	Wages Expense	410,000
Cash		410,000

9. October 25: Payment of Insurance Premium

Date	Particulars	Debit (Rs.)
Oct 25	Insurance Expense	29,600

Date	Particulars	Debit (Rs.)
Cash		29,600

10. October 26: Payment to Creditors

Date	Particulars	Debit (Rs.)	Credit (Rs.)
Oct 26	Accounts Payable	240,000	
Cash		240,000	

11. October 28: Cash Received for Job Completed

Date	Particulars	Debit (Rs.)
Oct 28	Cash	140,000
Revenue from Services		140,000

12. October 29: Invoice Received for Truck Expenses

Date	Particulars	Debit (Rs.)
Oct 29	Truck Expenses	41,000
Accounts Payable		41,000

13. October 29: Payment of Miscellaneous Expenses

Date	Particulars	Debit (Rs.)	Credit (Rs.)
Oct 29	Miscellaneous Expense	33,000	
Cash		33,000	

14. October 30: Wages Paid to Employees

Date	Particulars	Debit (Rs.)
Oct 30	Wages Expense	430,000
Cash		430,000

15. October 31: Owner's Cash Withdrawal

Date	Particulars	Debit (Rs.)
Oct 31	Mr. Bilal's Drawing	300,000
Cash		300,000

Posting Journal Entries to Ledger Accounts

Cash Account

Debit Entries	Credit Entries
2,000,000 (Investment)	70,000 (Supplies Purchase)
120,000 (Cash for Job)	1,000,000 (Truck Purchase)
140,000 (Cash for Job)	75,000 (Rent Payment)
410,000 (Wages Payment)	
29,600 (Insurance)	
240,000 (Payment to Creditors)	
33,000 (Miscellaneous)	
430,000 (Wages Payment)	
300,000 (Withdrawal)	
Total: 2,260,000	Total: 2,805,600

Accounts Payable

Debit Entries	Credit Entries
240,000 (Payment)	150,000 (Equipment Purchase)
41,000 (Truck Expenses)	
Total: 240,000	Total: 191,000

Mr. Bilal's Capital Account

Debit Entries	Credit Entries
2,300,000 (Investment)	
Total: 2,300,000	

Revenues from Services

Debit Entries	Credit Entries
120,000 (Job Completed)	
140,000 (Job Completed)	
Total:	Total: 260,000

Wages Expenses and Other Expenses

- Wages Expense:

- Debit: 410,000 (Oct 23), 430,000 (Oct 30)
- Miscellaneous Expense:
 - Debit: 33,000 (Oct 29)
- Rent Expense:
 - Debit: 75,000 (Oct 18)

Trial Balance as of October 31, 2024

Trial Balance	Debit (Rs.)
Cash	2,805,600
Accounts Payable	191,000
Mr. Bilal's Capital	2,300,000
Revenues from Services	
Wages Expense	410,000
Equipment	300,000
Truck	2,200,000
Supplies	330,000
Insurance Expense	29,600
Total	5,265,200

Conclusion

The above entries detail the essential steps undertaken in maintaining effective financial records for Mr. Noman's business, covering all relevant transactions, with supporting ledger accounts and a trial balance. This framework provides a comprehensive overview of the business's financial position for the month of October 2024.

Q. 4: Trial Balance Extraction and Adjustments

Trial Balance for Mr. Ahmed as of December 31, 2024

Trial Balance	Debit (Rs.)
Cash	500,000
Accounts Receivable	1,000,000
Inventory	700,000
Office Equipment	460,000
Insurance	60,000
Office Supplies	120,000

Trial Balance	Debit (Rs.)
Rent Expenses	90,000
Office Salary Expenses	20,000
Ahmed's Capital	
Ahmed's Drawings	50,000
Advertising Expenses	60,000
Delivery Expenses	20,000
Purchases	800,000
Sales	
Freight In	50,000
Purchases Returns	
Sales Returns	10,000
Total	4,700,000

Adjustments

To adjust the trial balance correctly, we first need to account for the following changes:

1. **Merchandise Inventory:** Final inventory is Rs. 850,000.
2. **Allowance for Depreciation on Office Equipment:** Rs. 60,000 must be accounted for.
3. **Unexpired Insurance:** Rs. 20,000 should be recorded as an asset.
4. **Office Supplies Consumed:** Rs. 30,000 must be accounted for as expenses.
5. **Outstanding Advertising Bill:** Rs. 10,000 needs to be recorded as an expense.

Adjusted Trial Balance Preparation

To adjust the balances, we will account for the adjustments mentioned above:

1. Adjust Inventory: Add [Inventory Final - Inventory Initial]: = 850,000 - 700,000 = +150,000
2. Adjust Depreciation: [Office Equipment -60,000]
3. Adjust Insurance: [Unexpired Insurance + 20,000]
4. Adjust Supplies: Record consumed as expenses == > + 30,000
5. Adjust Outstanding Advertising Bill: Record as an expense == > + 10,000

Adjusted Trial Balance After Adjustments

Adjusted Trial Balance	Debit (Rs.)
Cash	500,000
Accounts Receivable	1,000,000

Adjusted Trial Balance	Debit (Rs.)
Inventory	850,000
Office Equipment	460,000
Insurance	20,000
Office Supplies	90,000
Rent Expenses	90,000
Office Salary Expenses	20,000
Advertising Expenses	70,000
Delivery Expenses	20,000
Purchases	800,000
Sales	
Freight In	50,000
Purchases Returns	
Sales Returns	10,000
Depreciation Expense	60,000
Total	5,310,000

Conclusion

In conclusion, the adjustments enhance the overall trial balance accuracy for Mr. Ahmed's business as of December 31, 2024. Proper recording of transactions, along with adjustments, ensures that the financial statements reflect a true and fair view of the financial position of the business, facilitating better decision-making.

Q. 5: Depreciation Schedule Using the Units of Production Method

Background Information

On January 1, 2021, Mr. Noman purchased machinery for Rs. 139,000 with an estimated salvage value of Rs. 13,000 and a useful life of 5 years. The units produced for the first through fifth years are as follows:

- Year 1: 180,000 units
- Year 2: 156,000 units
- Year 3: 138,000 units
- Year 4: 126,000 units
- Year 5: 120,000 units

Calculating Depreciation

1. Determine Depreciable Cost

The depreciable cost is calculated as follows:

Depreciable Cost = Cost of Asset – Salvage Value

Depreciable Cost = 139,000 – 13,000 = 126,000
 $\text{Depreciable Cost} = 139,000 - 13,000 = 126,000$

2. Calculate the Depreciation per Unit

Next, we calculate the depreciation per unit produced:

$$\text{Depreciation per Unit} = \frac{\text{Depreciable Cost}}{\text{Total Estimated Units}}$$

The total estimated units over the useful life is 720,000 units:

$$\text{Depreciation per Unit} = \frac{126,000}{720,000} = 0.175 \text{ (Rs. per unit)}$$

3. Prepare Depreciation Schedule

Now, we can compute the annual depreciation expense based on the units produced each year:

Year	Units Produced	Depreciation Expense (Rs.)	Accumulated Depreciation (Rs.)	Book Value (Rs.)
2021	180,000	31,500	31,500	107,500
2022	156,000	27,300	58,800	80,200
2023	138,000	24,150	82,950	56,050
2024	126,000	22,050	105,000	34,000
2025	120,000	21,000	126,000	13,000

Conclusion

The depreciation schedule calculated using the units of production method illustrates how depreciation expense is allocated based on the actual production of the asset rather than time. This method provides a fair reflection of the asset's usage and wear and tear, ensuring accurate financial reporting.